IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

ROYAL INDEMNITY COMPANY	:	
	:	
v.	:	
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DELI BY FOODARAMA, INC., GLEN ROSENWALD, SPECIALTY INSURANCE AGENCY, INC., FIRST NATIONAL FINANCIAL SERVICES, INC., FIRST TRUST BANK, INC. LITO AND SONS CLEANERS, INC., HARLEYSVILLE MUTUAL INSURANCE COMPANY	:	**CIVIL ACTION**
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	:	**NO. 97-1267**
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M E M O R A N D U M

WALDMAN, J. **January 11, 2001**

Background

This is an insurance coverage dispute. Plaintiff seeks a declaration that a policy it issued to defendant Deli By Fooderama is void because of material misrepresentations made in securing coverage. Plaintiff has joined as defendants the insured, its principal, the managing agent which bound the coverage and the brokerage which presented the insurance application.[1]

Upon agreement of the parties, certain threshold issues were tried separately pursuant to Fed. R. Civ. P. 42(b). These

[1]Plaintiff also joined three other defendants, First Trust Bank, Lito and Harleysville, with tangential interests who elected not to participate in the litigation.

issues are whether misrepresentations were made to plaintiff in the course of securing coverage for Deli By Fooderama and, if so, whether any such misrepresentations were material and, if so, to which party are such misrepresentations attributable.

The resolution of these issues necessarily requires a determination of which testimony to credit. After a review of the testimony, the various exhibits and the applicable law, the court makes the following pertinent findings of fact and legal conclusions.

FINDINGS OF FACT

Plaintiff is a Delaware corporation with its principal place of business in Charlotte, North Carolina.

Defendant Deli by Foodarama, Inc. (Deli) is a Pennsylvania corporation which operated a restaurant at 1681 Grant Avenue in Philadelphia between 1985 and 1996.

Defendant Glen Rosenwald was majority shareholder, president and secretary of Deli, and personally managed the restaurant.

Defendant Specialty Insurance Agency, Inc. (Specialty) is a New Jersey corporation with its principal place of business in Manasquan, New Jersey.

Defendant First National Financial Services, Inc. (First National) is a Pennsylvania corporation with its principal place of business in Feasterville, Pa.

The amount in controversy exceeds $75,000, exclusive of interest and costs.

After graduating from Penn State University, Mr. Rosenwald worked from 1978 to 1985 for Foodarama, Inc., his family's business. During that period, he was responsible for the purchase of insurance and the handling of all insurance claims for Foodarama, Inc. From 1978 to 1996, Mr. Rosenwald also assisted his brothers and mother with the purchase of insurance and the handling of insurance claims for business which they owned and operated.

From the inception of Deli in 1985, Mr. Rosenwald was responsible for the purchase of insurance and the handling of all insurance claims for that company. Mr. Rosenwald typically purchased insurance for a one year term and then "shopped" each year for the best rate. Mr. Rosenwald was sophisticated about insurance.

From January 1994, Marc Grossman was employed by his father's insurance agency, the Martin Grossman Agency. Mr. Grossman knew the Rosenwald family and that they were involved in the restaurant business. Mr. Grossman specialized in placing insurance coverage for restaurants and identified Deli as a potential client.

Mr. Grossman determined that the anniversary date for Deli's insurance coverage was March 19, 1994 and arranged to meet

with Mr. Rosenwald in January 1994 to discuss insurance for Deli. The meeting took place in Mr. Rosenwald's office. Deli's bookkeeper was also present.

Mr. Grossman asked questions to obtain information necessary to solicit a quote for coverage, including questions about Deli's history of prior property, general liability and liquor claims. Mr. Rosenwald stated that there were no prior claims. Based on the information provided by Mr. Rosenwald, Mr Grossman prepared an application and sent it to Specialty for a quote. Specialty provided a quote, but Mr. Rosenwald ultimately chose not to place insurance through Mr. Grossman at that time.

In September 1994, the Martin Grossman Agency merged with First National which entered into a brokerage agreement with Specialty the following December. Under the agreement, First National agreed to submit insurance risks to Specialty for placement with insurers in return for commissions.

Under a 1988 agreement, Specialty was the managing agent for plaintiff Royal's "Restaurant Program," with the authority to solicit, underwrite, bind and issue policies covering restaurants in four northeastern states including Pennsylvania.

A telephone solicitor employed by First National arranged for another meeting between Mr. Grossman and Mr. Rosenwald in late January 1995 at Deli. The two met in a booth at the restaurant. Mr. Grossman again asked questions to obtain

information to solicit a quote. In response to questions about Deli's claims history, Mr. Rosenwald told Mr. Grossman that Deli had experienced no property, general liability or liquor liability claims in the five preceding years.

Based on the information provided by Mr. Rosenwald, Mr. Grossman prepared a restaurant application to telefax to Specialty for a quote. Mr. Rosenwald was not asked to sign the application as Mr. Grossman did not intend to bind coverage, but only to solicit a quote. Specialty reviewed the application and prepared a written quote which was presented to Mr. Rosenwald. He again decided not to place coverage through Mr. Grossman.

For the period of March 19, 1995 to March 19, 1996, Deli was insured by West American Insurance Company at a premium of $9,588 without liquor liability. West American sent a notice to Deli on January 11, 1996 stating that insurance coverage would not be renewed because of Deli's history of claims during the coverage year.[2]

[2]The form was captioned "Notice of Cancellation, Nonrenewal or Increase in Policy Premium." Mr. Rosenwald testified that at least initially he thought the notice pertained to an increase in the premium. This is difficult to credit in view of the unmistakable placement of an "x" only in the box next to "non-renewal." In any event, Mr. Rosenwald did not deny an understanding that some adverse action was being undertaken because of Deli's history of claims. The words "Loss history" clearly appear on the line next to "Reason(s) for cancellation or nonrenewal."

After receiving the notice of non-renewal, Mr. Rosenwald again met with Mr. Grossman in late January 1996. Mr. Grossman was accompanied by Nate Kleeman, president of First National. Mr. Grossman and Mr. Kleeman met with Mr. Rosenwald at Deli in a booth near the front of the restaurant. As Mr. Rosenwald was busy and leaving periodically to tend to business matters, the meeting lasted for about two hours.

Mr. Grossman brought the restaurant application from the prior year and an updated application form to the meeting. Mr. Grossman asked questions of Mr. Rosenwald to elicit information called for on the application form for submission to Specialty, and recorded the responses.

Mr. Rosenwald provided Messrs. Grossman and Kleeman with the name of his current carrier and the amount of the premium. He did not, however relate that he had received a notice of non-renewal from West American. Messrs. Grossman and Kleeman were left with the impression that West American was willing to renew the policy and that they were thus competing with that insurer and others for Deli's business.

Mr. Rosenwald told Messrs. Grossman and Kleeman that neither he nor Deli had any bankruptcies, foreclosures, tax liens or business failures, and that neither was involved in any litigation.[3]

[3]The question regarding litigation per se was addressed to personal or business litigation which could affect the stability of the restaurant, and not to insured liability claims which were addressed in another section of the application.

Mr. Rosenwald identified one pending lawsuit against Deli arising from a slip and fall, in response to a question regarding general liability claims. There were in fact at the time two lawsuits pending against Deli in the Court of Common Pleas of Philadelphia.

Mr. Rosenwald discussed his current coverage with Messrs. Grossman and Kleeman but declined to give them a copy of the West American policy. Mr. Rosenwald sought an increase in contents coverage from $265,000.00 to $350,000.00. When Mr. Kleeman suggested that Mr. Rosenwald obtain a formal appraisal of the contents, he declined. Mr. Rosenwald selected the amount of coverage for business income, general liability and liquor liability, and provided information about food and alcohol sales. Mr. Rosenwald never requested that the owner of the building in which the restaurant was a tenant be named as an additional insured.

Mr. Grossman asked whether Deli had experienced any property, general liability, liquor liability or umbrella claims during the past five years, all information required on the Specialty application. Mr. Rosenwald related that there was one general liability claim arising from the aforementioned slip and fall, and that there had been no property, liquor liability or umbrella claims during the period in question. During the prior five years Mr. Rosenwald, on behalf of Deli, had in fact

submitted twelve claims to insurers, including six to West American, for property damage or loss on which a total of $206,653 was ultimately paid. Three of these claims were for losses exceeding $15,000.

Mr. Grossman prepared the restaurant application from the information supplied by Mr. Rosenwald and telefaxed it to Specialty on January 31, 1996 along with a letter prepared by Mr. Rosenwald regarding the identified general liability claim and negligence suit. Based upon the information provided by Mr. Rosenwald, Mr. Grossman had written "none" on the line calling for property claims during the prior five years.[4]

Mr. Rosenwald was not asked to sign the application as the purpose at the time was not to bind coverage, but only to solicit a quote. Within a few weeks, Specialty quoted to Mr. Grossman by telephone a premium of $9,925.00 including liquor liability.

During this time, Dennis Bowman of the Loomis Agency in Ephrata, Pa. was engaged by Alan Cohen, the broker for Deli's West American policy, to place insurance coverage for Deli after receipt of the notice of non-renewal. Mr. Bowman concluded that

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[4]Mr. Rosenwald testified at his deposition that he was not asked about prior property claims. He testified at trial that he did not recall if he was asked about such claims. It is most unlikely that Messrs. Grossman and Kleeman would have persisted for two hours if they were not intent on asking each question in the application and eliciting the information called for.

he could not obtain insurance coverage for Deli in the standard market and would have to go to the excess market at about double the present premium. Mr. Bowman communicated this to Mr. Rosenwald by letter in mid-February 1996. This information was not shared with First National.

After receiving the quote from Specialty, Mr. Grossman prepared an insurance proposal for Deli dated March 1, 1996. Messrs. Grossman and Kleeman then met with Mr. Rosenwald to review the proposal during the first week of March 1996. Mr. Rosenwald contacted Mr. Grossman several days later to state that the initial quote was too high. Mr. Grossman went back to Specialty and obtained a reduced quote of $9,325.00 which included a $175.00 inspection fee. Mr. Rosenwald agreed to accept the coverage if the inspection fee were waived. Specialty agreed and provided a quote of $9,150.00 without inspection. Mr. Rosenwald then agreed to accept the coverage and on March 18, 1996 gave Mr. Kleeman a down-payment on the premium. Mr. Grossman then telefaxed a request to Specialty to bind coverage on March 19, 1996, and it did so on behalf of Royal effective as of that date.

Throughout this process, Deli, through Mr. Rosenwald, looked to First National to secure coverage on Deli's behalf for the best premium from any appropriate insurer.

By letter of March 28, 1996 to First National, Specialty requested an explanation of several negative items in a Dun & Bradstreet (D&B) report it had obtained on Deli, including notations of four lawsuits and a judgment against Deli. Mr. Kleeman delivered that letter and the D&B report to Mr. Rosenwald shortly after it was received, and subsequently attempted to obtained an explanation without success. When three follow-up requests also failed to produce a response, Specialty issued a notice of cancellation on May 7, 1996, effective July 8, 1996.

Upon receipt of the notice, Mr. Rosenwald called Mr. Kleeman to ask what could be done to reinstate coverage. Mr. Kleeman explained that the notice of cancellation resulted from the unexplained information in the D&B report. Mr. Rosenwald stated that he had lost his copy of the report and asked Mr. Kleeman to send another copy which he did on May 14, 1996. Mr. Kleeman then met with Mr. Rosenwald at the restaurant where he provided an explanation for each entry on the D&B report as Mr. Kleeman made notes. Mr. Kleeman then took a sheet of stationery with a Deli letterhead on which he typed the responses of Mr. Rosenwald to the negative information in the D&B report. Mr. Rosenwald reviewed the letter, found it to be accurate and signed it. Mr. Kleeman sent the letter to Specialty where it was reviewed by James Drummond, the assigned underwriter. After Mr. Kleeman relayed some further explanation of the responses, Mr.

Drummond was satisfied and Specialty reinstated the policy as of May 30, 1996.

Deli then made a claim to Royal for a theft loss occurring on May 12, 1996. Deli made a claim to Royal for damages resulting from a fire on July 11, 1996. Shortly after the fire, Mr. Rosenwald received a notice of cancellation of the non-renewed West American policy, with an effective date of August 26, 1996. Mr. Rosenwald then assumed he had coverage under both policies and ultimately sued West American on June 4, 1997 for damages resulting from the fire when it denied coverage. He nevertheless executed and submitted a Sworn Statement in Proof of Loss on October 29, 1996 for presentation to plaintiff representing that Deli had no other insurance of any kind for the fire loss.[5]

Plaintiff's policy contained an express unambiguous provision that coverage would be "void" if the insured intentionally concealed or misrepresented any material fact in presenting a claim.

Mr. Rosenwald is aware that several family businesses are insured today through First National. He has never advised

[5]Mr. Rosenwald testified that he "must have overlooked" the West American policy. This seems quite unlikely in view of his general attentiveness to the matter of insurance and the discussions with counsel to which he testified leading to the filing of a claim with and then lawsuit against West American barely six months after execution of the statement in proof of loss.

family members to cease doing business with that agency for reasons of competence, integrity or otherwise.

Neither Mr. Grossman nor Mr. Kleeman had knowledge of Deli's actual loss history until after the fire of July 11, 1996. First National earned a 15% commission on the placement of the insurance for Deli which it was obligated to return when Royal rescinded the policy and refunded the premium.

Specialty never demanded the insured's signature on the Deli application. The company generally attempts to obtain the insured's signature once coverage is bound, but it often does not and a signature is not required. Binding coverage without an insured's signature on an application is a common practice in the commercial insurance industry. Many insurers today take the pertinent information, provide quotes and bind coverage via computer with no signature.

Plaintiff's "Restaurant Program" operated on a small profit margin and thus only businesses deemed to be very good risks were accepted. Plaintiff's underwriting guidelines expressly excluded from eligibility establishments with "claim frequency" or which "have sustained a loss in excess of $15,000 in the last five years."

Specialty, through Mr. Drummond, relied on the claims history information in the Deli application in quoting a premium and binding coverage. Had Mr. Drummond been aware of Deli's

actual property claim history or the related non-renewal by West American, he would not have approved coverage at any premium.[6]

Conclusions of Law

The court has subject matter jurisdiction pursuant to 28 U.S.C. § 1332(a).

The subject insurance policy was issued in Pennsylvania to a Pennsylvania insured for a business and property located in Pennsylvania, and it is uncontested that the insurance contract is governed by the substantive law of Pennsylvania. See Travelers Ins. Co. v. Fantozzi, 825 F. Supp. 80, 84 (E.D. Pa. 1993); Hughes v. Prudential Lines, Inc., 624 A.2d 1063, 1066 n.2 (Pa. Super.), app. denied, 633 A.2d 152 (Pa. 1993).

Under Pennsylvania law, an insurer may void an insurance policy upon a showing that the insured knowingly or in bad faith made a misrepresentation in the insurance application which was material to the risk insured. See Matinchek v. John Alden Life Inc. Co., 93 F.3d 96, 102 (3d Cir. 1996); Coolspring Stone Supply Co., Inc. v. American States Life Ins. Co., 10 F.3d 144, 148 (3d Cir. 1993); United National Ins. Co. v. J.H. France Refractories Co., 612 A.2d 1371, 1377 (Pa. Super. 1992). Such a misrepresentation in an application must be proven by clear and convincing evidence. See Batka v. Liberty Mut. Fire Ins. Co.,

[6]Royal was not an excess lines carrier.

704 F.2d 684, 687 (3d Cir. 1983); Rohm and Haas Co. v. Continental Cas. Co., 732 A.2d 1236, 1251-52 (Pa. Super. 1999).

A misrepresentation is material if disclosure of the truth would have caused the insurer to refuse coverage of the risk or to require a greater premium. See New York Life Ins. Co. v. Johnson, 923 F.2d 279, 281 (3d Cir. 1991). The misrepresentation, however, need not relate to the loss actually sustained. See American Franklin Life Ins. Co. v. Galled, 776 F. Supp. 1054, 1060 n.2 (E.D. Pa. 1991).

In stating that Deli had no property claims over the prior five year period, Mr. Rosenwald clearly made a material misrepresentation on which Specialty relied in binding coverage. See, e.g., Metropolitan Property and Liability Ins. Co. v. Insurance Com'r. of Penna., 580 A.2d 300, 303 (Pa. 1990) (three undisclosed prior claims for losses totalling $17,000 was "certainly material"). In making this statement barely two weeks after receipt of the West American notice of non-renewal for claims frequency, Mr. Rosenwald must have known that he was speaking falsely.

First National was operating as an agent of Deli in recording Mr. Rosenwald's responses on the application and forwarding it to Specialty. See Kairys v. Aetna Casualty and Surety Co., 461 A.2d 269, 275-76 (Pa. Super. 1983).

Plaintiff has established by clear and convincing evidence that it would have refused to issue the subject policy but for a material misrepresentation knowingly made by Mr. Rosenwald and attributable to Deli, and only to Deli.[7]

Plaintiff is entitled to rescind or void the policy unless it waived such right by continuing coverage with knowledge of Deli's misrepresentation, a matter to be determined consistent with the parties' stipulation and order of December 29, 1999.

[7]It appears that Mr. Rosenwald, who assumed Deli had coverage under the West American policy, also intended to misrepresent the availability of other insurance when he executed a statement in proof of loss for submission to plaintiff. Nevertheless, the essence of a misrepresentation is a statement of fact which is false. See Wittekamp v. Gulf & Western, Inc., 991 f.2d 1137, 1142 (3d Cir.), cert. denied, 510 U.S. 917 (1993); Gibbs v. Ernst, 647 A.2d 882, 889 (Pa. 1994). The West American cancellation notice with an August 1996 effective date was apparently issued by mistake and it appears that coverage actually lapsed in March 1996. While Mr. Rosenwald's conduct in this regard may bear generally on his credibility, the court cannot determine on the record presented whether the failure to identify other coverage was in fact a material misrepresentation.

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O R D E R

AND NOW, this day of January, 2001, consistent with the accompanying memorandum, which shall be filed of record herewith, and the court's order of December 29, 1999, **IT IS HEREBY ORDERED** that the parties shall submit by February 15, 2001 proposed findings of fact and conclusions of law for the remaining issues herein.

BY THE COURT:

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JAY C. WALDMAN, J.